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C O N F I D E N T I A L SECTION 01 OF 03 RABAT 000109

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TAGS: EFIN ECON MA
SUBJECT: 2009 BUDGET HIGHLIGHTS GOM'S CONTINUING ROOM TO MANEUVER

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Classified By: Econ Counselor Stuart Smith, Reasons 1.4 b/d.

¶1. (SBU) Summary: Morocco's 2009 budget, the first prepared by the government of Abbas El-Fassi, breaks little new ground in comparison with its predecessors. The budget maintains a strong focus on social issues, which account for 53 percent of spending. Reduced subsidy spending has enabled the government to increase the resources allocated to public investment, with the goal of counterbalancing expected downturns in foreign investment, remittences, and exports as a result of the global financial crisis. Other measures to support growth include reinforcement of spending on key weaknesses in Morocco's business environment. These include additional resources for the justice sector and support for new anti-corruption and competition agencies. The budget, with this increased spending and continuation of reduction in income tax rates, shows that Morocco's strong fiscal performance in recent years gives the government room to maneuver, even in an economic downturn. The "Alliance of Economists" of the Prime Minister's own Istiqlal party has called for even more spending, however, arguing that the government has focused too much on reducing Morocco's indebtedness, which it argues is already manageable at 53.6 percent of GDP. Meanwhile, parliament's inability to affect the budget underscores its lack of power. End Summary.

¶2. (U) Budget Outline: The global budget envisions an increase in revenue of 24 percent to USD 35.2 billion and an increase of expenditures of 23 percent to USD 36.7 billion (when autonomous activities and special Treasury accounts are included), leaving the country with a "revenue shortfall" of approximately USD 1.5 billion (or MAD 13 billion). (Note: The actual deficit is budgeted to be larger, at USD 2.6 billion, or approximately 3 percent of GDP, as budget revenues include some loans and expenditures include paying off some of Morocco's existing debts. End Note.) While predicted revenue increases appear large, they are actually less ambitious than they first appear. Actual tax revenue in 2008 exceeded budget projections by 20 percent, so that the actual increase over the revenues realized in 2008 is only 3 percent.

¶3. (U) The budget is framed to address two primary goals: maintaining an elevated level of growth in the face of the global economic downturn, while also addressing Morocco's lagging performance on a number of key social indicators. Social sectors account for 53 percent of all spending, and have increased by USD 1.4 billion over the 2008 budget. Priority areas include particularly education (USD 5.5 billion or 16 percent of spending is devoted to education), public health, housing, urban development, and youth and sports.

¶4. (U) Though the majority of state resources in the budget are devoted to social goals, the government's public focus has centered more on its planned measures to support growth. These include:

-- Increasing investment: direct state investment will rise 25 percent to USD 5.4 billion, while overall investment (including that by public enterprises and the Hassan II Fund) will be three times that at USD 16 billion. Principal projects include accelerating investment for the full range of transportation infrastructure, and developing new poles for specific industries across Morocco. These include for the chemical industry (near Jorf Lasfar), fishery canning industry (Agadir), offshoring (Oujda, Fes, and Marrakech), and agro-industry (Meknes, Berkane, and Beni-Mellal), as well as extension of existing industrial zones near the Tanger Med port.

-- Reinforcement of the purchasing power of Moroccan citizens: extension of the "Moukawalati" ("My Enterprise") program, which helps young entrepreneurs win micro-financing for their business projects; an increase in public sector salaries (a 9 percent increase in the government's salary bill, though recruitment will be strictly limited to bring the overall civil service salary/GDP ratio down to the average rate for comparable countries); increase in family allowances; reduction in top tax rates (now down to 40 percent from the previous top rate of 42 percent) and an increase in the income floor for taxation from USD 2,857 to USD 3,333.

-- Support for exports: Continued reduction in import duties to reduce the cost of manufacturing inputs; encouragement of the capitalization of small and medium-sized enterprises by allowing them to reduce their profit tax by 10 percent;

creation of a special USD 59.5 million fund to support exports; and simplification of customs procedures.

-- Diversification of the sources of growth through invigoration of sectoral strategies for agriculture (spending will rise 58 percent to USD 800 million to implement the "Plan Maroc Vert"), water, energy, and phosphates, and support for other sectors.

-- Improvement of the business climate through acceleration of reform of the justice sector (which will see a 22 percent budget increase), support for the new Central Anti-Corruption Agency and the Competition Council, and creation of both a new Economic and Social Council and a single investment promotion agency.

¶5. (SBU) A number of issues remain to be addressed. While subsidy spending will fall to USD 3.4 billion from last year's USD 5.2 billion, as a result of the recent fall in the price of oil and other primary commodities, the promised reform of the subsidy system to focus aid on needy populations is tackled only incrementally. The government will launch a limited USD 59.5 million program to channel assistance directly to the poorest Moroccans. For now the compensation system itself remains largely unchanged, however, with the bulk of spending devoted to petroleum products, whose benefit primarily reaches more favored segments of the population.

¶6. (SBU) Perhaps because of the ongoing public focus on the international economic conjuncture and its implications for Morocco, only muted comment has surrounded the budget. At the time of its debate in Parliament, opposition MPs particularly targeted the government's decision to raise consumption taxes on basic consumer staples, rather than to increase taxes on alcohol. They also pressed for the income floor for taxation to be raised further. As usual, however, the government ruled most of these proposals out of order, on the basis of constitutional provisions that preclude deputies

from proposing amendments that either reduce government revenues or result in an additional burden on the public. It did, however, agree to raise the floor for imposition of income tax from USD 3,200 to USD 3,300.

¶7. (C) Aside from standard opposition denunciation of this parliamentary tactic, the most significant critique has come from the "Alliance of Economists" associated with the Prime Minister's own Istiqlal party. That group, headed by former Tourism Minister Adil Douiri, termed the budget "prudent and comfortable" but suggested that the government had room to be significantly more aggressive in seeking to attain its goal of keeping Morocco's growth rate up in the current international climate. In a recent meeting with us, Douiri suggested that the continuing focus on reducing Morocco's overall indebtedness is misplaced. Government debt is down to 53.6 percent of GDP, he noted, and the government has been at or near a balanced budget in each of the last two years. Such a budget policy is not appropriate for a developing country like Morocco, he argued. Instead, the government should ramp up spending on key sectors like housing and manufacturing and be willing to tolerate a deficit of 3-4 percent of GDP. The key change in Morocco's economic performance in recent years, Douiri pointed out, is that average annual non-agricultural growth has been raised from 3 to 5 percent. With exports likely to take a hit this year, he suggested that this improved performance will be difficult to maintain, and that the government could do even more to pick up the slack. In the Alliance's view, middle and low-income housing are the sectors where additional government spending would have the largest impact. Similarly, while expressing skepticism that government spending can reverse a business cycle, he argued that spending to support Morocco's manufacturing base through the downturn would leave it ready to resume exporting when conditions improve.

¶8. (C) Comment: Given that in addition to Douiri, a former Minister, the Alliance is composed primarily of young Istiqlal Ministers (including Economic and General Affairs' Nizar Baraka, Housing's Ahmed Hejira, and Transport's Karim Ghellab) its critique is more than a little ironic. Douiri stressed that while he closely coordinates his messaging with the party, the Alliance's role is to be out in front of the government and "to sow the seeds" for future policy decisions. This allows the party, which is just one part of the governing coalition, to keep its distance from Alliance recommendations, if it wishes. In this case, government movement in the Alliance's direction is likely if revenue

performance remains strong and if continued low oil prices also free up additional resources. Whether this will occur will only become evident over the course of the year. New figures released in late January, however, show that Morocco enters 2009 in a strong fiscal position: after a year (2007) in which an expected deficit turned into a balanced budget, analysts now anticipate that the 2008 budget will return a deficit far below its budgeted level of 3 percent of GDP, and may in fact yield a surplus, thanks to strong revenue performance. Baraka, in his presentation last week at Davos, highlighted this achievement of a deficit "below 1 percent of GDP," in the face of subsidy spending that reached 5 percent of GDP, as an indication of the "Moroccan exception." Overall, the 2009 Moroccan budget appears to be framed to leave the government room on the upside if revenues exceed forecasts, something that would not hurt the governing coalition electorally as local elections approach later this year. End Comment.

¶9. (U) Principal Budget Figures

(Note: Budget figures are given in Billion MAD; USD 1= MAD 8.4, approximately. End Note.)

EXPENDITURES	2009	Increase percentage
Government operations	17.96	21
Personnel/salaries	9.00	13
Material	3.01	25
Common Charges		
Compensation	4.04	
(includes 5 billion in arrears from 2008)		
Unforeseen Expenses	0.36	
Pension Contributions	1.29	
Investment	5.38	25
Debt Service	6.88	21
Domestic Debt	6.04	40
capital	4.20	76
interest	1.84	-5
External Debt	0.84	-39
capital	0.52	-51
interest	0.32	-2
TOTAL General State Budget	30.21	22
State Services Managed Autonomously	0.25	27
Special Treasury Accounts	6.26	11
TOTAL Overall GOM Budget	36.72	23
REVENUES		
Direct Taxes	8.63	25
Company tax (IS)	5.08	45
Income tax (IR)	3.45	5
Customs Revenue	1.65	8
Indirect taxes	7.46	20
Registration/Stamp taxes	1.52	26
Revenue from State Enterprises	1.19	45
Loans, grants	7.50	27
Privatization Revenue	0.36	
TOTAL GENERAL REVENUE	28.64	22
Revenues from Autonomous Activities	0.25	27
Revenue from Special Treasury Accounts	6.28	11
TOTAL BUDGET REVENUE	35.18	24
DEFICIT	1.55	

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